

MEMORANDUM FOR:

DCI

[redacted] has some specific ideas
on the economic competition he would like
to share with you, if you have
about 15 min tomorrow.

[redacted] wants addresses three
good agenda items. Please let me know
if you would like anything else.

CC:DDCI
D/OPP

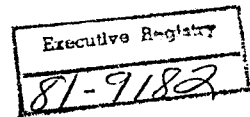
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THE DIRECTOR OF CENTRAL INTELLIGENCE

WASHINGTON, D.C. 20505

NFAC #7951-81
7 December 1981

National Intelligence Council

MEMORANDUM FOR: Director of Central Intelligence

VIA: Chairman, National Intelligence Council *HSR*FROM:
National Intelligence Officer for Economics

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SUBJECT: Your Meeting with the President's Economic Policy
Advisory Board on Thursday, 10 December

A. You might broach three topics, depending on the amount of time you have:

1. A brief report from you on increasing Soviet economic difficulties, the growing use of imports of goods and technology from the West to relieve Soviet economic problems, and the links between East-West economic relations and Soviet military power.

2. A brief introduction to the planned global Economic Estimate for 1982-83, and solicitation of views from the Board members.

3. Solicitation of help in guiding CIA/NFAC research on the key long range issues of economic competitiveness and industrial technology.

Soviet Economic Dependence

B. On the topic of Soviet economic problems and dependence, you may want to refer to the main points of the SNIE and the additional work under way on Western reactions to US initiatives in CoCom. It would be very useful to have the views of Board members on these points.

Global Estimate

C. With respect to the Global Estimate, our general thinking to date is as follows:

1. Our purpose in preparing such an estimate is not to present

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forecasts of economic trends, but rather to give the policy level of our Government perspective on contingencies which may affect economic developments and on the interactions between economic, political, and military events. In other words, we hope to give them a better idea of what to worry about in the context of developing national policy.

2. We expect to spend little time describing forecasts, although we hope to do enough analysis to gain some understanding of what drives these forecasts and what could change them.

3. We have been talking to many people both in the government and in the private sector; at this stage we plan to look at the following contingencies:

a. In the macro-economic area:

- a fairly severe recession in the US and Western Europe through the first half of next year, followed by very slow recovery;
- alternatively, a shift in the major European countries to expansionary policies leading to rapid economic recovery and accelerated inflation.

b. With respect to oil

- a heating up of the Iran/Iraq war leading to an interruption of Persian Gulf oil, and/or
- the war ends, leading to a large increase in Iranian and Iraqi oil production.

c. We have not found any commodity other than oil which, given likely general world market conditions in the next year to two, is a reasonable candidate for creating a significant economic problem.

d. We, like others, are worried about the potential for a major financial crisis, due, for example, to the collapse of a major Euro-dollar bank, and a mismanagement of the fallout from this collapse. But we have not found a good handle to deal with this possibility and would very much appreciate any ideas the Board members may have to guide our thinking and analysis.

e. Some of the more interesting scenarios we will be looking at would result from a combination of circumstances. For example, a combination of slow economic growth with a recovery of Iranian and Iraqi oil production could cause the demand for Saudi oil to become so depressed that the Saudis are unable to

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prevent a drop in the nominal price of oil. In any event, it would be difficult for them to engineer large enough cuts in production to clear the market, either by themselves, or with the cooperation of other countries. I might add that the real price of oil is likely to decline in any event, even if the nominal price does not.

4. Apart from the economic contingencies themselves, we will be looking at their implications for the economic policies of foreign countries and for our own policy interests.

a. There is obviously great concern about the impact of economic recession and large-scale unemployment in Europe on trade policies. A surge of protectionism may result in substantially tighter restrictions on European imports from Japan, LDCs and even the United States. The new MTN initiatives may get a very poor start.

b. Reactions to the inevitably large Japanese trade and current account surpluses will be strong both here and abroad. We will look at what the Japanese may or may not do in response to these reactions.

c. Dissatisfaction with economic developments and in some cases with US policies may feed back to other aspects of US relations with Europe and perhaps Japan. For example, the degree of support the US has obtained in Europe on East-West economic issues, already quite weak, may become even smaller.

5. These are just some preliminary thoughts. We would appreciate the Board members' concerns as to problems for the next couple of years.

Long-Term Competitiveness

D. Longer term problems are of particularly great concern. In particular, there is the gnawing problem of declining US competitiveness and sluggish productivity.

1. Unfortunately, this is a subject on which we have not done much work so far, and the rest of the government is no better off. We have done good analysis on energy, but only bits and pieces on industrial developments abroad, and on key factors affecting US competitiveness, especially major changes in technology. We are participating in a study of trends in high technology industries sponsored by the Department of Commerce, and are laying out our own program of long-term research in the area of industrial competitiveness. This program will include studies of:

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a. Foreign Government Industrial and Technological Strategies.

- The first study, due by mid-year 1982, will be on Japanese Industrial Strategy.

b. Likely future competitive environment in key industries and technologies abroad. These studies will include:

- Japan's Computer Industry
- The Outlook for Industrial Automation
- Japanese Robotics
- International Competition for Commercial Aircraft
- Japan's Fiber Optics Industry
- Advent of the Mini Car Market

c. The key factors affecting productivity and competitiveness in major foreign countries. These studies will include:

- Industrial Investment in the 1980s: A Look at Capital Markets
- OECD Countries: Review and Analysis of Slowdown in Productivity Growth
- Major Developed Countries: Savings Rates and Public Policy
- OECD Countries: Demographics, Labor Force and Youth Employment in the 1980s
- Newly Industrializing Countries: Implications of Shifts in Production Structure
- Western Europe: Regional and Sectoral Trends in Unemployment

2. Our research program will take several years to complete, but important parts, including those just mentioned, will be available next year. We would very much appreciate the Board members' guidance, both collectively and individually, on this complex matter.

Backup Support

E. Attached is background material on each of the three major topics:

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- the SNIE on Soviet dependence;
- the outline for the Global Economic Estimate.

F. [] and I will be out of town on Thursday, but []
[] will be available to give you further support, and/or to
accompany you if you like. Should you want someone to brief on the Soviet
estimate, I would suggest [] who was the principal drafter of the
SNIE. Should you want to go into the NFAC research program on Foreign
Industrial Competition, I would suggest you bring [] of OGI with
you.

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Attachments,
As stated

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Advisory Board on Thursday, 10 December

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